

STATE OF TENNESSEE

Office of the Attorney General



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April 26, 2002

Mr. David Waddell
Executive Secretary
Tennessee Regulatory Authority
460 James Robertson Parkway
Nashville, TN 37243-0505

Re: United Cities Gas Petition for Approval
of New or Revised Franchise, Agreements with
Kingsport, Bristol, Morristown and Maury County
Docket No. 00-00562

Dear Mr. Waddell:

Enclosed is an original and thirteen copies of the Reply Brief and Motion to Strike of the Attorney General in the above-referenced matter. Copies are being furnished to counsel of record for interested parties.

Sincerely,

TIMOTHY C. PHILLIPS
Assistant Attorney General

cc: Counsel of Record
54686

POSTED
4/29/02

**BEFORE THE TENNESSEE REGULATORY AUTHORITY
NASHVILLE, TENNESSEE**

IN RE:

UNITED CITIES GAS PETITION FOR
APPROVAL OF NEW OR REVISED
FRANCHISE AGREEMENTS WITH
KINGSPORT, BRISTOL, MORRISTOWN
AND MAURY COUNTY

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) Docket No. 00-00562
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REPLY BRIEF AND MOTION TO STRIKE OF THE ATTORNEY GENERAL

The Tennessee Attorney General, through the Consumer Advocate and Protection Division ("Attorney General"), files this motion to strike and brief in response to the "REPLY OF THE CITY OF MORRISTOWN, TENNESSEE TO ATTORNEY GENERAL'S POST HEARING BRIEF", filed with the Tennessee Regulatory Authority ("Authority") on April 18, 2002 and received by the Attorney General on April 24, 2002.

The Attorney General is in receipt of the reply brief filed by the City of Morristown. The Attorney General objects to the late filing of this brief and moves this Authority to strike same. The reply brief was filed and served outside the time period prescribed by the hearing officer in this matter.

The manner in which the City of Morristown interjects this late filing is prejudicial to the interest of the customers of United Cities Gas. Further, there are specific problems with the assertions made in the reply brief. If the Authority is not inclined to strike the reply brief then the

Attorney General requests that the Authority consider the following thoughts.

At page 6 of Morristown's reply brief, the city refers to the testimony of a United Cities Gas representative as supporting the assertion that as a result of public hearings held by the city, the city delayed its investigation into determining whether or not to take over the gas supply service from United Cities Gas. The problem with this assertion is two-fold. First, the actual testimony does not bare out this conclusion. Second, a representative from United Cities Gas does not possess the personal knowledge to draw conclusions as to why the City of Morristown passed the resolution referenced in the testimony.

The City of Morristown claims at page 6 of the brief that there were "true negotiations" over the franchise fee. Such characterizations of the testimony have little worth, unless supported by the testimony. The Attorney General asks that the hearing officer review the record in its entirety, noting specifically the numerous references to the record thus far by the Attorney General which clearly demonstrate that both the City of Bristol and the City of Morristown simply imposed upon United Cities, and ultimately its customers, a certain franchise fee arbitrarily determined. In response to the demand for franchise fees from each city, United Cities Gas conceded the point without further interaction and certainly without any "give and take" which might suggest "true negotiations." The fact that the franchise fees in these petitions were set without "contentious" discussion is rather obvious as noted at page 6 of Morristown's reply brief. The simple fact is that there were no negotiations whether contentious or otherwise. It is equally obvious that United Cities Gas customers did not participate in this process. Assuming *arguendo*, that there were actually no consumer complaints regarding the franchise fees the cities have imposed on the customers of United Cities Gas, the reason for the lack of complaints is

equally obvious. The testimony in this matter is clear: there is simply no way for the customers of United Cities Gas to know they are being charged a franchise fee. The fees are not itemized on the bills so that the customers would notice them. Further, there was no consumer education regarding the fee.

At page 7 of the reply brief, the City of Morristown brings up an interesting point. There is little contention among the parties that the cities should receive compensation for allowing United Cities Gas to use the rights of way. This is a natural result of the proper application of the policies and legal framework involved. However, to arbitrarily set a franchise fee without any evidence suggesting its reasonableness potentially leads to over-compensation of the cities for the use of the rights of way. The cities do not impose a fee based on actual costs, a reasonable rental fee or the market value of the rights of way. Instead, United Cities Gas and the cities reference the decisions in *Nashville Gas and Heating Company v. City of Nashville*, and *Lewis v. Nashville Gas and Heating Company* as authority for their proposition that a franchise fee may be “definite sum arbitrarily selected.” However, this appeal to legal precedence is misleading because neither decision deals with a franchise fee requiring the approval of the Authority.

Further, both decisions that the proponents of the franchise fee rely on predate significant tax law changes. Taxation is a governmental function. A city may not levy a tax in its proprietary capacity. Both United Cities and Morristown fail to grasp the concept that it is the act involved that answers the question of which functional capacity the city is exercising. If the city levies a tax, it does so in its governmental capacity rather than its role as proprietor.

Moreover, the cities involved are prohibited by the legislature from instituting a franchise tax. A municipality may not tax indiscriminately. *See* Tenn. Code Ann. § 67-4-401. Under

general revenue law, municipalities may not tax gas, water, or electric companies. Tenn. Code Ann. § 67-4-404. Furthermore, municipalities do not have the power to levy any kind of franchise tax. See Tenn. Code Ann. § 67-4-2102. This is not a case where the city's actions affect only it as a corporation and another party. Instead, the ordinances at issue reach directly to the citizens of the municipalities involved. As such, the measure is a tax. Moreover, the cases the proponents of the franchise fee cite are clearly distinguishable in that the franchise fees *Nashville Gas and Heating Company v. City of Nashville*, and *Lewis v. Nashville Gas and Heating Company* were reviewed by the Tennessee Supreme Court prior to the passage of the statute allowing United Cities Gas to pass along the franchise fees to its customers.

United Cities Gas and the cities offer the outdated rationale found in the *Nashville Gas and Heating Company v. City of Nashville*, and *Lewis v. Nashville Gas and Heating Company* decisions as an exception from the general principle that cities may not impose such taxes. It is the proponents' obligation to fit these franchise fees into that exception.

Factually, there is no proof in the record showing that "true negotiations" took place. Further, the party paying the fees were not even at the table for the negotiations.

These franchise fees are passed along to the customers of United Cities Gas even though these customers were not represented during the alleged negotiations between the cities and United Cities Gas. The City of Morristown's claims to the contrary skirts the issue at the very core of these proceedings. Two parties set a fee at an arbitrary rate that is collected from a third party who had no voice at the bargaining table. Both the City of Morristown and the City of Bristol clearly have conflicting interests involved. As a direct result of the dual roles of these governmental units, the interest of the customers of United Cities Gas has been pushed aside in

favor of the interest of the majority of the citizens of the Cities of Bristol and Morristown. The interest of the customers of United Cities Gas have been pushed behind the interest of the City of Bristol and the City of Morristown in satisfying their own needs, in particular, growing their tax base.

The Attorney General requests that this Authority consider both the applicable law and the sound policy considerations embodied in the case law and statutory scheme applicable to franchise fees and franchise taxes. For instance, a city should not be allowed through the orders of the Authority to impose a tax disguised as a franchise fee. Further, this Authority should not permit the Cities of Bristol and Morristown to unfairly discriminate against a small portion of its population in imposing a tax only on the customers of United Cities Gas.

Review of this matter goes deeper than the decisions in *Nashville Gas and Heating Company v. City of Nashville*, and *Lewis v. Nashville Gas and Heating Company*. In considering what is good public policy, this Authority should take into consideration the disproportionate impact these franchise fees have on the customers of United Cities Gas. The sole argument offered by the City of Morristown in suggesting that its franchise fee is in the best interest of the public is insufficient. The fact that a city uses a franchise fee for the sole purpose of holding down other taxes that it charges the citizenry in general is a detriment to the public interest rather than a benefit. It is, at its base, unfair for the cities involved in this matter to disproportionately tax a small group of its citizens who are similarly situated to the majority of the citizens, except for the fact that they heat their homes with gas.

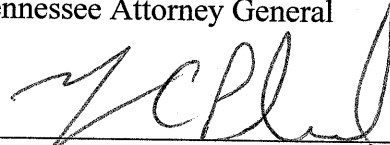
Finally, in the discussion of the franchise fees at issue in this docket it is critical to recognize that, even under the incorrect view of the law regarding taxation proposed by the

proponents of these franchise fees, demonstrating that the cities were operating in their proprietary capacity is merely the threshold which the proponents of this franchise fee must cross.¹ The cities and United Cities Gas must demonstrate to this Authority that these franchise fees are necessary and proper for the public convenience and properly conserves the public interest. It should be kept in mind that there was no review by either the Public Service Commission or the Tennessee Regulatory Authority of the franchise fees at issue in the *Nashville Gas and Heating Company v. City of Nashville*, and *Lewis v. Nashville Gas and Heating Company* decisions. Under the theory proposed by United Cities Gas and the cities emphasized in the City of Morristown's reply brief, any fee arbitrarily set would be appropriate as long as United Cities Gas agreed to collect it from its customers. Given this attitude, it falls upon this Authority to temper the decisions of the City of Morristown and the City of Bristol with sound public policy, and a reasonable approach to setting the franchise fees.

¹The Attorney General does not concede that this threshold has been met. Even under the analysis offered by the proponents of the franchise fees of the decisions in *Nashville Gas and Heating Company v. City of Nashville*, and *Lewis v. Nashville Gas and Heating Company* the requisite negotiations did not take place.

Respectfully submitted,

PAUL G. SUMMERS
Tennessee Attorney General

A handwritten signature in dark ink, appearing to read 'T. Phillips', is written over a horizontal line.

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Certificate of Service

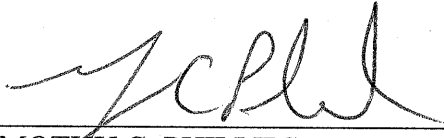
I hereby certify that a true and correct copy of the foregoing was served via U.S. Mail on
April 26, 2002 on the following:

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